



Deloitte Legal commercial law webinar

COVID-19 business impact – how to manage your commercial agreements during and post lockdown

Executive summary

As the global and local economies continue to deal with the coronavirus (COVID-19), the pandemic has resulted in significant disruptions to ongoing commercial transactions. It is therefore imperative for organisations to pay particular attention to the potential impact and consequences of these disruptions on its agreed contractual terms. This entails amongst others, having measures in place for effective contract management and enforcement as well as contract governance.

Below is a summary of the topics discussed.

Commercial law key themes:

1. Force Majeure

Force *majeure* clauses contain contractually agreed upon procedures that will apply when a party's ability to perform under a contract is negatively impacted by an event outside of its control. These clauses typically provide for the temporary suspension of the parties' respective contractual obligations for the duration of the force *majeure* event, provided that the specific criteria in the force *majeure* clause are met. These clauses are usually defined quite broadly and do not always contain an exhaustive list of examples. If the event falls within the ambit of the clause, the affected party can exercise its rights in terms of the clause. If it does not, the clause finds no application to the relevant circumstances and the affected party would need to rely on its common law rights or other clauses in the contract for relief.

2. COVID-19 as a force *majeure* event

When analysing whether the COVID-19 pandemic would fall within the definition of a force *majeure* event contemplated in the relevant contract, it is important to understand what is causing the party's inability to perform. In a South African context, in particular during the COVID-19 pandemic, the question is whether the COVID-19 pandemic is the force *majeure* event or whether it is the regulations published in terms of the Disaster Management Act, 2002 ("**Regulations**"). In most cases, unless one tests positive for the COVID-19 disease and is hospitalised and cannot perform under a contract, the relevant force *majeure* event causing the inability to perform is not the COVID-19 pandemic itself, but in most cases, the regulations as these restrict movement of persons and prohibit certain services or operations from being performed.

The regulations would typically fall within the list of force *majeure* events in existing contracts, as these generally include government action/regulations, or even lockdowns specifically, as force *majeure* events, and it would be regarded as having been reasonably unforeseeable at the time that the contract was entered into. If the affected party is able to show that the event falls within the ambit of the force *majeure* clause, then it will need to follow the process set out in the contract regarding notification to the other party and any further requirements as stipulated in the contract. If the notice is given on time, this typically has the result of suspending the parties' obligations with effect from the date of the notice (or the event arising) depending on the wording. This typically means that neither party is required to perform, but the parties can regulate the specific performance/obligation that is affected.

It is important to note that a force *majeure* event does not subsist indefinitely and generally requires the party affected by the force *majeure* event to notify the other party as soon as performance becomes possible again.

Lastly, the force *majeure* clause will usually stipulate, in favour of the other party, that if the force *majeure* event endures for longer than a specific prescribed period, the other party is entitled to terminate the contract on written notice to the other. Sometimes both parties can terminate. The terms of the contract, particularly the notice periods, should be carefully considered and complied with.

3. No force *majeure* clause, no problem

In the absence of a force *majeure* clause dealing with the particular event in question, or where the event falls outside of the ambit of the force *majeure* clause, the common law will apply. In such circumstances, the common law concept of supervening impossibility of performance may be relied upon by a party when facing a claim for specific performance from the counterparty, provided that specific factual circumstances exist.

The usual consequence of supervening impossibility is that the obligations of both parties are extinguished and the contract terminates. This is typically the position where the supervening impossibility is permanent. Where the supervening impossibility is only temporary, the obligations are not extinguished, but merely suspended. However, if it becomes unreasonable in the circumstances for the other party to wait for suspended performance, it may have a right to cancel the contract.

4. Variations to contracts

Under the South African law, parties have freedom to contract on terms agreed between them, subject to limited restrictions. Accordingly, parties to an existing contract are, in general, able to agree to renegotiate or vary the terms of that contract on terms acceptable to the parties and subject to any specific terms in the contract dealing with such renegotiation or variation. Where a contract is silent on the issue of force *majeure*, it may then be in the best interests of the parties to attempt to renegotiate the terms of the contract that are impacted by the force *majeure* event, in order to reach an amicable position for both parties in the circumstances.

5. Withholding of rental under commercial lease agreements

In the case of the COVID-19 pandemic and regulations, although these may impact the ability of the lessee to pay rental as a result of its inability to generate an income through sales, this is not an objective and absolute impossibility of performance. Given that in such an instance, the lessee's obligation to pay the rental is not rendered objectively impossible, it may not be able to invoke a force *majeure* clause (depending on the exact wording of the clause). In such instances, the common law principle of remission of rental is relevant. This principle is different from force *majeure* and is based on the principle of reciprocity of obligations.

In the case of such reciprocal obligations, the common law position is that a reduction in the performance of one obligation, amounts to a proportionate reduction in the performance of the reciprocal obligation. That is, if the lessee is deprived of its use and enjoyment of the property (being the lessor's obligation), then it may claim a remission of rental payable to the lessor (being the lessee's obligation) proportionate to its reduction in such use and enjoyment, depending on the circumstances giving rise to such deprivation.

6. Mergers and acquisitions (M&A) transactions during the COVID-19 pandemic

Those that are in pre-signing or pre-closing stages will undoubtedly be subject to the COVID-19 pandemic endurance test. Draft sale and purchase agreements will be scrutinised particularly in respect of safe guarding principles such as material adverse change clauses. In respect of transactions already concluded, there is a high risk of disputes arising as businesses become unable or unwilling to perform existing contractual obligations.

Nothing in law restricts the conclusion of new contracts, as they can be executed electronically. Depending on the specific business, the COVID-19 pandemic may have various practical implications on M&A transactions including business valuations, setting up and accessing data rooms to conduct a due diligence investigation, obtaining the relevant regulatory approvals and securing finance, all of which can impact the actual closing and implementation of a transaction.

7. Respond, recover and thrive

The pressure to modernise in the digital age has for many been regarded as a luxury, resulting in some businesses now finding themselves isolated from their systems, employees and information. The COVID-19 pandemic has made it clear that businesses need to invest in their systems and technology in particular, with clients/customers requiring near real time solutions. The use of technology can assist with various business drivers,

including; but not limited to; optimising business operations, managing business risk, predicting new market opportunities and improving regulatory compliance.

Contact us:

Sibongile Solombela

Director: Deloitte Legal

ssolombela@deloitte.co.za

Samantha Tumber

Associate Director: Deloitte Legal

stumber@deloitte.co.za

Tessa Quaker

Associate Director: Deloitte Legal

tquaker@deloitte.co.za

Hanno Kruger

Senior Manager: Deloitte Legal

hakruger@deloitte.co.za

Get in touch



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